UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF TENNESSEE
SOUTHERN DIVISION

In re:

No. 93-13246
Chapter 7

SHERIDAN T. JOHNSTON
VICKI S. JOHNSTON

Debtors

RICHARD P. JAHN, JR., TRUSTEE

Plaintiff

v.

Adversary Proceeding
No. 95-1156

LIMITED FEW MOTORCYCLE CLUB, INC., and ROBERT A. KLEIN, as Agent for Limited Few Motorcycle Club, Inc., and Individually

Defendants

Appearances: Jerry Weeks, Jahn & Weeks, Chattanooga, Tennessee, Attorney for Plaintiff

Ashley Ownby, Cleveland, Tennessee, Attorney for Defendants

R. Thomas Stinnett, United States Bankruptcy Judge

Sheridan and Karen Johnston filed bankruptcy in August 1993. The plaintiff, Mr. Jahn, was appointed trustee. He brought this suit against one of Mr. Johnston's creditors, Limited Few Motorcycle Club, and its secretary-treasurer, Robert Klein. The complaint alleges that the defendants are liable for the value of a 1989 Harley-Davidson motorcycle that Mr. Johnston owned when he filed bankruptcy but which was sold during the bankruptcy case for $4,500. Limited Few and Mr. Klein contend they cannot be liable for more than the $500 they actually received from the sale proceeds. They also contend they are not liable for any amount because they were good faith subsequent transferees. The court finds the facts as follows.

In August 1993 Mr. Johnston owed Limited Few an old debt of $4,700. He attempted to secure the debt by giving Limited Few a security interest in his 1989 Harley-Davidson motorcycle. He signed both a security agreement and an application to note Limited Few's lien on the certificate of title. The security agreement is dated August 1, 1993. The application to note the lien is dated August 19, 1993.

The certificate of title shows Bowater Employees Credit Union as the first lienholder, but the credit union had executed the release on the back of the title certificate in 1991. Limited Few is shown as the second lienholder, but the notation is handwritten. Limited Few admits this did not perfect the security interest, and the security interest was never perfected by a proper notation on the certificate of title.

The Johnstons filed their bankruptcy case on August 31, 1993, shortly after Mr. Johnston gave Limited Few the security interest. In their bankruptcy case the

Johnstons filed lists of their property and debts, as required by law. They listed the motorcycle as subject to Limited Few's security interest.

The bankruptcy trustee sent a letter to Limited Few to the attention of Mr. Klein. The letter is dated September 28, 1993. The letter made two points. First, the trustee would not abandon the motorcycle without seeing documents to prove Limited Few's security interest. Second, Limited Few should present the documents within ten days by filing a proof of claim with the security interest, note, and certificate of title attached.

The trustee sent Limited Few a second letter dated February 11, 1994. The trustee again requested documentary proof of Limited Few's security interest. He went on to say, "Otherwise, I will assume you do not have a perfected lien on the motorcycle, and will take appropriate steps to sell it."

The clerk's office received Limited Few's proof of claim on February 16, 1994. The proof of claim included copies of the security agreement, the certificate of title, and the application to note Limited Few's security interest on the certificate of title. Mr. Klein signed the proof of claim as secretary and treasurer of Limited Few.

Robert E. Travis, Jr., bought the motorcycle shortly after Limited Few filed its proof of claim. The terms of the sale were handwritten on a preprinted invoice from Matrix Cycle Supply. The invoice is dated February 24, 1994. It provides as follows:

> Sold to Matrix Cycle Supply
> owner Robert E. Travis, Jr.

[signature of Robert E. Travis Jr.]
one '89 HD vin # 1HD1BJL45KY019035
for the sum of 4500.00
Four Thousand Five Hundred $^{00}/_{100}$
Dep 500^{00} ck # 0454
Balance due upon delivery
with title being free an [sic]
Clear of all liens
seller SHERIDAN T. JOHNSTON
[signature of Sheridan T. Johnson]
buyer Robert E. Travis, Jr.
[signature of Robert E. Travis, Jr.]
*sold as is

Mr. Klein testified that Limited Few never had possession of the motorcycle but did have possession of the certificate of title for two months or so. He stated that he understood the bankruptcy case was dismissed or completed in December 1993. He learned of the sale around February 24, 1994. Limited Few had the title certificate at that time. He turned it over to Mr. Johnston after receiving the $500, but not immediately afterward. He did not know who was buying the motorcycle and did not care where the $500 came from. Mr. Klein denied knowing the motorcycle was property of the bankruptcy estate at the time of the sale. According to Mr. Klein, he first learned this when he received a third letter from the bankruptcy trustee, but that was in March 1994 after the sale was completed.

DISCUSSION

Section 549 of the Bankruptcy Code allows the trustee to avoid a transfer of property if (1) the property was property of the bankruptcy estate, (2) the transfer occurred after the filing of the bankruptcy petition, and (3) the transfer was not authorized by the Bankruptcy Code or by the court. 11 U.S.C. § 549.

The proceeds from the sale of the motorcycle were as much property of the bankruptcy estate as the motorcycle itself. 11 U.S.C. §541(a)(6); *Cossitt v. First American State Bank (In re Fort Dodge Creamery Co.)*, 121 B.R. 831 (Bankr. N. D. Iowa 1990); *Albion Production Credit Association v. Langley (In re Langley)*, 30 B.R. 595, 10 Bankr. Ct. Dec. 784 (Bankr. N. D. Ind. 1983); *see also Lowe v. Yochem (In re Reed)*, 184 B.R. 733, 27 Bankr. Ct. Dec. 730 (Bankr. W. D. Tex. 1995); *In re Walston*, 190 B.R. 855 (Bankr. S. D. Ill. 1996).

The transfer occurred after the Johnstons filed bankruptcy and was not authorized by statute or by the court. Thus, the transfer is avoidable by the trustee. Limited Few and Mr. Klein argue that they are not liable or they are liable only for the $500 received by Limited Few. They rely on § 550 of the Bankruptcy Code. 11 U.S.C. § 550.

Section 550 establishes two categories of defendants. In the first category are initial transferees and entities for whose benefit the transfer was made. 11 U.S.C. § 550(a)(1) & (b). In the second category are subsequent transferees — transferees who received the property from an initial transferee or a later transferee. 11 U.S.C. § 550(a)(2) & (b).

Under §550(b)(1), the trustee cannot recover from a subsequent transferee who, in good faith, gave value in return for the transfer and did not have knowledge of the

voidability of the transfer. Limited Few and Mr. Klein contend they are protected by this statute.

The evidence did not show whether the $500 check was written to Limited Few or was written to Mr. Johnston and endorsed by him to Limited Few. If the latter, then Limited Few and Mr. Klein may have been subsequent transferees. But they are not protected by the statute because they did not receive the transfer in good faith.

Mr. Klein denied knowing the motorcycle was property of the bankruptcy estate at the time of the sale. Mr. Klein did not, however, deny receiving the letters from the trustee. The court infers that the trustee's second letter provoked Mr. Klein to file the proof of claim. The letter was dated five days before the proof of claim was received. Since the proof of claim was received before the sale, Mr. Klein must have received the second letter before the sale. The letter said the trustee would take the motorcycle and sell it unless Limited Few proved its security interest. After receiving this letter Mr. Klein must have known that the trustee had the paramount claim to the motorcycle. Likewise, Mr. Klein must have known that Mr. Johnston should not be selling the motorcycle for his own benefit and should not be paying them to turn over the title certificate. In this situation Limited Few and Mr. Klein did not receive the transfer in good faith. *See Lugo v. De Jesus Saez (In re De Jesus Saez)*, 20 B.R. 19 (Bankr. D. P. R. 1982); *Groupe v. Hill (In re Hill)*, 156 B.R. 998, 29 Collier Bankr. Cas. 2d 637 (Bankr. N. D. Ill. 1993); *Friedman v. Vinas (In re Trauger)*, 109 B.R. 502 (Bankr. S. D. Fla. 1989); *see also Mosier v. Goodwin (In re Goodwin)*, 115 B.R. 674, 20 Bankr. Ct. Dec. 1007 (Bankr. C. D. Cal. 1990); *Robinson v.*

Home Savings of America (In re Concord Sr. Housing Foundation), 94 B.R. 180, 20 Collier Bankr. Cas. 2d 430 (Bankr. C. D. Cal. 1988).

This brings the court to the question of whether the defendants can be liable for $4,500 — the full value of the motorcycle — even though they received only $500 from the sale.

Under § 550 a trustee can recover from a transferee or an entity for whose benefit the transfer was made. 11 U.S.C. § 550(a). In this case the trustee is attempting to recover the value of the motorcycle, not the motorcycle itself. Section 550 appears to limit the recovery from a transferee to the value of the property it received. On the other hand, the person for whose benefit the transfer was made may be liable for the full value of the property even though it did not receive the property. This leads to the trustee's main argument that the defendants are liable for $4,500. The trustee contends they are liable for $4,500 as entities for whose benefit the transfer was made because they admitted to being entities for whose benefit the transfer was made. The trustee relies on a stipulation by the defendants in the Joint Pretrial Statement. They stipulated that the sale by Mr. Johnston occurred for their benefit.

If the trustee's argument is correct, then the Joint Pretrial Statement is internally inconsistent. Part III of the Joint Pretrial Statement sets out the defendants' defenses. Paragraph A sets out the defense under § 550(b)(1) that the defendants were good faith subsequent transferees. An "entity for whose benefit such transfer was made" does not have this defense. 11 U.S.C. § 550(a)(1) & (b)(1). Thus, the defendants could not admit liability under § 550(a)(1) as entities for whose benefit the transfer was made and also rely on the defense under § 550(b) that they were good faith subsequent transferees.

The trustee's view of the defendant's stipulation contradicts another defense set out in the Joint Pretrial Statement. Paragraph B of Part III says, "Value received by Defendants was $500 and that is the entire amount the Trustee can recover from Defendants." In light of this defense, the defendants obviously did not intend to admit liability for the $4,500 unless they proved the defense that they were good faith subsequent transferees.

Finally, the trustee's argument assumes that an entity for whose benefit the transfer was made will *always* be liable for the full value of the property transferred to someone else. This is often true, but the statute does not require that result. Consider two examples.

Debtor owes Scofflaw $3,000. Scofflaw owes Wagner $3,500. Scofflaw tells the debtor to pay the $3,000 to Wagner. In Debtor's bankruptcy case his payment to Wagner is avoidable. Scofflaw is a person for whose benefit the transfer was made. He received the full benefit of the transfer, since it paid $3,000 of his debt to Wagner, and he can be liable for $3,000.

Change the facts so that Debtor also owes $1,000 to Wagner. He pays the $3,000 to Wagner, but this time it pays his $1,000 debt to Wagner and $2,000 of his debt to Scofflaw by paying $2,000 of Scofflaw's debt to Wagner. Scofflaw again is a person for whose benefit the transfer was made. Can he be liable for the full $3,000 even though the benefit to him was only $2,000? Some courts might say so, but the court doubts this is the correct result. 2 *David G. Epstein, et al., Bankruptcy* § 6-88 at 243-244 (1992). Scofflaw was the entity for whose benefit such transfer — meaning the transfer of $2,000 — was

made. He was not the person for whose benefit the other $1,000 was transferred. The court does not think that the entity for whose benefit the transfer was made is always liable for the value of all the property transferred.

In summary, the court disagrees with the trustee's view of the Joint Pretrial Statement. The defendants did not stipulate that they would be liable for the full $4,500 unless they prevailed on the defense that they were good faith subsequent transferees.

The trustee failed to prove any other ground for holding the defendants liable for more than the $500 they received. This leaves the question of whether Mr. Klein is also liable. Limited Few was the transferee and received the direct, measurable benefit of the $500 payment. Mr. Klein was acting on behalf of Limited Few. There may be situations in which the court should impose liability on the employee, agent, or officer of a corporation who received an avoidable transfer on its behalf. The trustee, however, did not prove any ground for Mr. Klein's personal liability.

The trustee requested that attorney's fees be awarded to him, but presented no basis and no authority for an award of attorney's fees. The trustee also requested that he be awarded the costs of this cause. Because the court is of the opinion this litigation could have been completely avoided if Limited Few had responded to the trustee's initial correspondence, the costs shall be adjudged against Limited Few.

The court will enter judgment against Limited Few in accordance with this memorandum, which constitutes the court's findings of fact and conclusions of law as required by Fed. R. Bankr. P. 7052.

At Chattanooga, Tennessee.

BY THE COURT

R. THOMAS STINNETT
UNITED STATES BANKRUPTCY JUDGE

[entered 4/12/96]

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Defendants

ORDER OF JUDGMENT

In accordance with the Memorandum Opinion entered by the court,

It is ORDERED that the plaintiff shall have and recover from defendant, Limited Few Motorcycle Club, Inc., a judgment in the amount of Five Hundred Dollars ($500.00) together with interest thereon from and after February 24, 1994, plus costs.

ENTER:

BY THE COURT

R. THOMAS STINNETT
U.S. BANKRUPTCY JUDGE

[entered 4/12/96]